

FIRST DIVISION

[G.R. No. 99398. January 26, 2001]

CHESTER BABST, *petitioner*, vs. COURT OF APPEALS, BANK OF THE PHILIPPINE ISLANDS, ELIZALDE STEEL CONSOLIDATED, INC., and PACIFIC MULTI-COMMERCIAL CORPORATION, *respondents*.

[G.R. No. 104625. January 26, 2001]

ELIZALDE STEEL CONSOLIDATED, INC., *petitioner*, vs. COURT OF APPEALS, BANK OF THE PHILIPPINE ISLANDS, PACIFIC MULTI-COMMERCIAL CORPORATION and CHESTER BABST, *respondents*.

D E C I S I O N

YNARES-SANTIAGO, J.:

These consolidated petitions seek the review of the Decision dated April 29, 1991 of the Court of Appeals in CA-G.R. CV No. 17282^[1] entitled, Bank of the Philippine Islands, *Plaintiff-Appellee* versus Elizalde Steel Consolidated, Inc., Pacific Multi-Commercial Corporation, and Chester G. Babst, *Defendants-Appellants*.

The complaint was commenced principally to enforce payment of a promissory note and three domestic letters of credit which Elizalde Steel Consolidated, Inc. (ELISCON) executed and opened with the Commercial Bank and Trust Company (CBTC).

On June 8, 1973, ELISCON obtained from CBTC a loan in the amount of P8,015,900.84, with interest at the rate of 14% per annum, evidenced by a promissory note.^[2] ELISCON defaulted in its payments, leaving an outstanding indebtedness in the amount of P2,795,240.67 as of October 31, 1982.^[3]

The letters of credit, on the other hand, were opened for ELISCON by CBTC using the credit facilities of Pacific Multi-Commercial Corporation (MULTI) with the said bank, pursuant to the Resolution of the Board of Directors of MULTI adopted on August 31, 1977 which reads:

WHEREAS, at least 90% of the Companys gross sales is generated by the sale of tin-plates manufactured by Elizalde Steel Consolidated, Inc.;

WHEREAS, it is to the best interests of the Company to continue handling said tin-plate line;

WHEREAS, Elizalde Steel Consolidated, Inc. has requested the assistance of the Company in obtaining credit facilities to enable it to maintain the present level of its tin-plate manufacturing output and the Company is willing to extend said requested assistance;

NOW, THEREFORE, for and in consideration of the foregoing premises ---

BE IT RESOLVED AS IT IS HEREBY RESOLVED, That the PRESIDENT & GENERAL MANAGER, ANTONIO ROXAS CHUA, be, as he is hereby empowered to allow and authorize ELIZALDE STEEL CONSOLIDATED, INC. to avail and make use of the Credit Line of PACIFIC MULTI-COMMERCIAL CORPORATION with the COMMERCIAL BANK & TRUST COMPANY OF THE PHILIPPINES, Makati, Metro Manila;

RESOLVED, FURTHER, That the Pacific Multi-Commercial Corporation guarantee, as it does hereby guarantee, solidarily, the payment of the corresponding Letters of Credit upon maturity of the same;

RESOLVED, FINALLY, That copies of this resolution be furnished the Commercial Bank & Trust Company of the Philippines, Makati, Metro Manila, for their information. ^[4]

Subsequently, on September 26, 1978, Antonio Roxas Chua and Chester G. Babst executed a Continuing Suretyship, ^[5] whereby they bound themselves jointly and severally liable to pay any existing indebtedness of MULTI to CBTC to the extent of P8,000,000.00 each.

Sometime in October 1978, CBTC opened for ELISCON in favor of National Steel Corporation three (3) domestic letters of credit in the amounts of P1,946,805.73, ^[6] P1,702,869.32 ^[7] and P200,307.72, ^[8] respectively, which ELISCON used to purchase tin black plates from National Steel Corporation. ELISCON defaulted in its obligation to pay the amounts of the letters of credit, leaving an outstanding account, as of October 31, 1982, in the total amount of P3,963,372.08. ^[9]

On December 22, 1980, the Bank of the Philippine Islands (BPI) and CBTC entered into a merger, wherein BPI, as the surviving corporation, acquired all the assets and assumed all the liabilities of CBTC. ^[10]

Meanwhile, ELISCON encountered financial difficulties and became heavily indebted to the Development Bank of the Philippines (DBP). In order to settle its obligations, ELISCON proposed to convey to DBP by way of *dacion en pago* all its fixed assets mortgaged with DBP, as payment for its total indebtedness in the amount of P201,181,833.16. On December 28, 1978, ELISCON and DBP executed a Deed of Cession of Property in Payment of Debt. ^[11]

In June 1981, ELISCON called its creditors to a meeting to announce the take-over by DBP of its assets.

In October 1981, DBP formally took over the assets of ELISCON, including its indebtedness to BPI. Thereafter, DBP proposed formulas for the settlement of all of ELISCON's obligations to its creditors, but BPI expressly rejected the formula submitted to it for not being acceptable. ^[12]

Consequently, on January 17, 1983, BPI, as successor-in-interest of CBTC, instituted with the Regional Trial Court of Makati, Branch 147, a complaint ^[13] for sum of money against ELISCON, MULTI and Babst, which was docketed as Civil Case No. 49226.

ELISCON, in its Answer, ^[14] argued that the complaint was premature since DBP had made serious efforts to settle its obligations with BPI.

Babst also filed his Answer alleging that he signed the Continuing Suretyship on the understanding that it covers only obligations which MULTI incurred solely for its benefit and not for any third party liability, and he had no knowledge or information of any transaction between MULTI and ELISCON. ^[15]

MULTI, for its part, denied knowledge of the merger between BPI and CBTC, and averred that the guaranty under its board resolution did not cover purchases made by ELISCON in the form of trust receipts. It set up a cross-claim against ELISCON alleging that the latter should be held liable for any judgment which the court may render against it in favor of BPI. ^[16]

On February 20, 1987, the trial court rendered its Decision,^[17] the dispositive portion of which reads:

WHEREFORE, in view of all the foregoing, the Court hereby renders judgment in favor of the plaintiff and against all the defendants:

- 1) Ordering defendant ELISCON to pay the plaintiff the amount of P2,795,240.67 due on the promissory note, Annex A of the Complaint as of 31 October 1982 and the amount of P3,963,372.08 due on the three (3) domestic letters of credit, also as of 31 October 1982;
- 2) Ordering defendant ELISCON to pay the plaintiff interests and related charges on the principal of said promissory note of P2,102,232.02 at the rates provided in said note from and after 31 October 1982 until full payment thereof, and on the principal of the three (3) domestic letters of credit of P3,564,349.25 interests and related charges at the rates provided in said letters of credit, from and after 31 October 1982 until full payment;
- 3) Ordering defendant ELISCON to pay interests at the legal rate on all interests and related charges but unpaid as of the filing of this complaint, until full payment thereof;
- 4) Ordering defendant ELISCON to pay attorneys fees equivalent to 10% of the total amount due under the preceding paragraphs;
- 5) Ordering defendants Pacific Multi-Commercial Corporation and defendant Chester Babst to pay, jointly and severally with defendant ELISCON, the total sum of P3,963,372.08 due on the three (3) domestic letters of credit as of 31 October 1982 with interests and related charges on the principal amount of P3,963,372.08 at the rates provided in said letters of credit from 30 October 1982 until fully paid, but to the extent of not more than P8,000,000.00 in the case of defendant Chester Babst;
- 6) Ordering defendant Pacific Multi-Commercial Corporation and defendant Chester Babst to pay, jointly and severally plaintiff interests at the legal rate on all interests and related charges already accrued but unpaid on said three (3) domestic letters of credit as of the date of the filing of this Complaint until full payment thereof;
- 7) Ordering defendant Pacific Multi-Commercial Corporation and defendant Chester Babst to pay, jointly and severally, attorneys fees of not less than 10% of the total amount due under paragraphs 5 and 6 hereof. With costs.

SO ORDERED.

In due time, ELISCON, MULTI and Babst filed their respective notices of appeal.^[18]

On April 29, 1991, the Court of Appeals rendered the appealed Decision as follows:

WHEREFORE, the judgment appealed from is MODIFIED, to now read (with the underlining to show the principal changes from the decision of the lower court) thus:

- 1) Ordering appellant ELISCON to pay the appellee BPI the amount of P2,731,005.60 due on the promissory note, Annex A of the Complaint as of 31 October 1982 and the amount of P3,963,372.08 due on the three (3) domestic letters of credit, also as of 31 October 1982;
- 2) Ordering appellant ELISCON to pay the appellee BPI interests and related charges on the principal of said promissory note of P2,102,232.02 at the rates provided in said note from and after 31 October 1982 until full payment thereof, and on the principal of the three (3) domestic letters of credit of P3,564,349.25 interests and related charges at the rates provided in said letters of credit, from and after 31 October 1982 until full payment;
- 3) Ordering appellant ELISCON to pay appellee BPI interest at the legal rate on all interests and related charges but unpaid as of the filing of this complaint, until full payment thereof;

4) Ordering appellant Pacific Multi-Commercial Corporation and appellant Chester G. Babst to pay appellee BPI, jointly and severally with appellant ELISCON, the total sum of P3,963,372.08 due on the three (3) domestic letters of credit as of 31 October 1982 with interest and related charges on the principal amount of P3,963,372.08 at the rates provided in said letters of credit from 30 October 1982 until fully paid, but to the extent of not more than P8,000,000.00 in the case of defendant Chester Babst;

5) Ordering appellant Pacific Multi-Commercial Corporation and defendant Chester Babst to pay, jointly and severally, appellee BPI interests at the legal rate on all interests and related charges already accrued but unpaid on said three (3) domestic letters of credit as of the date of the filing of this Complaint until full payment thereof and the plaintiffs lawyers fees in the nominal amount of P200,000.00;

6) Ordering appellant ELISCON to reimburse appellants Pacific Multi-Commercial Corporation and Chester Babst whatever amount they shall have paid in said Eliscons behalf particularly referring to the three (3) letters of credit as of 31 October 1982 and other related charges.

No costs.

SO ORDERED. ^[19]

ELISCON filed a Motion for Reconsideration of the Decision of the Court of Appeals which was, however, denied in a Resolution dated March 9, 1992. ^[20] Subsequently, ELISCON filed a petition for review on certiorari, docketed as G.R. No. 104625, on the following grounds:

- A. THE BANK OF THE PHILIPPINE ISLANDS IS NOT ENTITLED TO RECOVER FROM PETITIONER ELISCON THE LATTERS OBLIGATION WITH COMMERCIAL BANK AND TRUST COMPANY (CBTC)
- B. THERE WAS A VALID NOVATION OF THE CONTRACT BETWEEN ELISCON AND BPI THERE BEING A PRIOR CONSENT TO AND APPROVAL BY BPI OF THE SUBSTITUTION BY DBP AS DEBTOR IN LIEU OF THE ORIGINAL DEBTOR, ELISCON, THEREBY RELEASING ELISCON FROM ITS OBLIGATION TO BPI.
- C. PACIFIC MULTI COMMERCIAL CORPORATION AND CHESTER BABST CANNOT LAWFULLY RECOVER FROM ELISCON WHATEVER AMOUNT THEY MAY BE REQUIRED TO PAY TO BPI AS SURETIES OF ELISCONS OBLIGATION TO BPI; THEIR CAUSE OF ACTION MUST BE DIRECTED AGAINST DBP AS THE NEWLY SUBSTITUTED DEBTOR IN PLACE OF ELISCON.
- D. THE DBP TAKEOVER OF THE ENTIRE ELISCON AMOUNTED TO AN ACT OF GOVERNMENT WHICH WAS A FORTUITOUS EVENT EXCULPATING ELISCON FROM FURTHER LIABILITIES TO RESPONDENT BPI.
- E. PETITIONER ELISCON SHOULD NOT BE HELD LIABLE TO PAY RESPONDENT BPI THE AMOUNTS STATED IN THE DISPOSITIVE PORTION OF RESPONDENT COURT OF APPEALS DECISION. ^[21]

BPI filed its Comment ^[22] raising the following arguments, to wit:

1. Respondent BPI is legally entitled to recover from ELISCON, MULTI and Babst the past due obligations with CBTC prior to the merger of BPI with CBTC.
2. BPI did not give its consent to the DBP take-over of ELISCON. Hence, no valid novation has been effected.
3. Express consent of creditor to substitution should be recorded in the books.
4. Petitioner Chester G. Babst and respondent MULTI are jointly and solidarily liable to BPI for the unpaid letters of credit of ELISCON.

5. The question of the liability of ELISCON to BPI has been clearly established.

6. Since MULTI and Chester G. Babst are guarantors of the debts incurred by ELISCON, they may recover from the latter what they may have paid for on account of that guaranty.

Chester Babst filed a Comment with Manifestation,^[23] wherein he contends that the suretyship agreement he executed with Antonio Roxas Chua was in favor of MULTI; and that there is nothing therein which authorizes MULTI, in turn, to guarantee the obligations of ELISCON.

In its Comment,^[24] MULTI maintained that inasmuch as BPI had full knowledge of the purpose of the meeting in June 1981, wherein the takeover by DBP of ELISCON was announced, it was incumbent upon the said bank to formally communicate its objection to the assumption of ELISCONs liabilities by DBP in answer to the call for the meeting. Moreover, there was no showing that the availment by ELISCON of MULTIs credit facilities with CBTC, which was supposedly guaranteed by Antonio Roxas Chua, was indeed authorized by the latter pursuant to the resolution of the Board of Directors of MULTI.

In compliance with this Courts Resolution dated March 17, 1993,^[25] the parties submitted their respective memoranda.

Meanwhile, in a petition for review filed with this Court, which was docketed as G.R. No. 99398, Chester Babst alleged that the Court of Appeals acted without jurisdiction and/or with grave abuse of discretion when:

1. IT AFFIRMED THE LOWER COURTS HOLDING THAT THERE WAS NO NOVATION INASMUCH AS RESPONDENT BANK OF THE PHILIPPINE ISLANDS (OR BPI) HAD PRIOR CONSENT TO AND APPROVAL OF THE SUBSTITUTION AS DEBTOR BY THE DEVELOPMENT BANK OF THE PHILIPPINES (OR DBP) IN THE PLACE OF ELIZALDE STEEL CONSOLIDATED, INC. (OR ELISCON) IN THE LATTERS OBLIGATION TO BPI.

2. IT CONFIRMED THE LOWER COURTS CONCLUSION THAT THERE WAS NO IMPLIED CONSENT OF THE CREDITOR BANK OF THE PHILIPPINE ISLANDS TO THE SUBSTITUTION BY DEVELOPMENT BANK OF THE PHILIPPINES OF THE ORIGINAL DEBTOR ELIZALDE STEEL CONSOLIDATED, INC.

3. IT AFFIRMED THE LOWER COURTS FINDING OF LACK OF MERIT OF THE CONTENTION OF ELISCON THAT THE FAILURE OF THE OFFICER OF BPI, WHO WAS PRESENT DURING THE MEETING OF ELISCONS CREDITORS IN JUNE 1981 TO VOICE HIS OBJECTION TO THE ANNOUNCED TAKEOVER BY THE DBP OF THE ASSETS OF ELISCON AND ASSUMPTION OF ITS LIABILITIES, CONSTITUTED AN IMPLIED CONSENT TO THE ASSUMPTION BY DBP OF THE OBLIGATIONS OF ELISCON TO BPI.

4. IN NOT TAKING JUDICIAL NOTICE THAT THE DBP TAKEOVER OF THE ENTIRE ELISCON WAS AN ACT OF GOVERNMENT CONSTITUTING A FORTUITOUS EVENT EXCULPATING ELISCON FROM ANY LIABILITY TO BPI.

5. IN NOT FINDING THAT THE DACION EN PAGO BETWEEN DBP AND BPI RELIEVED ELISCON, MULTI AND BABST OF ANY LIABILITY TO BPI.

6. IN FINDING THAT MULTI AND BABST BOUND THEMSELVES SOLIDARILY WITH ELISCON WITH RESPECT TO THE OBLIGATION INVOLVED HERE.

7. IN RENDERING JUDGMENT IN FAVOR OF BPI AND AGAINST ELISCON ORDERING THE LATTER TO PAY THE AMOUNTS STATED IN THE DISPOSITIVE PORTION OF THE DECISION; AND ORDERING PETITIONER AND MULTI TO PAY SAID AMOUNTS JOINTLY AND SEVERALLY WITH ELISCON.^[26]

Petitioner Babst alleged that DBP sold all of ELISCONs assets to the National Development Company, for the latter to take over and continue the operation of its business. On September 11, 1981, the Board of Governors of the DBP adopted Resolution No. 2817 which states that DBP shall enter into a contractual arrangement with NDC for the latter to pay ELISCONs creditors, including BPI in the amount of P4,015,534.54. This was followed by a Memorandum of Agreement executed on May 4, 1983 by and between DBP and NDC, wherein they stipulated, *inter alia*, that NDC shall pay to ELISCONs creditors, through DBP, the amount of P299,524,700.00. Among the creditors mentioned in the agreement was BPI, with a listed credit of P4,015,534.54.

Furthermore, petitioner Babst averred that the assets of ELISCON which were acquired by the DBP, and later transferred to the NDC, were placed under the Asset Privatization Trust pursuant to Proclamation No. 50, issued by then President Corazon C. Aquino on December 8, 1986.

In its Comment,^[27] BPI countered that by virtue of its merger with CBTC, it acquired all the latters rights and interest including all receivables; that in order to effect a valid novation by substitution of debtors, the consent of the creditor must be express; that in addition, the consent of BPI must appear in its books, it being a private corporation; that BPI intentionally did not consent to the assumption by DBP of the obligations of ELISCON because it wanted to preserve intact its causes of action and legal recourse against Pacific Multi-Commercial Corporation and Babst as sureties of ELISCON and not of DBP; that MULTI expressly bound itself solidarily for ELISCONs obligations to CBTC in its Resolution wherein it allowed the latter to use its credit facilities; and that the suretyship agreement executed by Babst does not exclude liabilities incurred by MULTI on behalf of third parties, such as ELISCON.

ELISCON likewise filed a Comment,^[28] wherein it manifested that of the seven errors raised by Babst in his petition, six are arguments which ELISCON itself raised in its previous pleadings. It is only the sixth assigned error --- that the Court of Appeals erred in finding that MULTI and Babst bound themselves solidarily with ELISCON --- that ELISCON takes exception to. More particularly, ELISCON pointed out the contradictory positions taken by Babst in admitting that he bound himself to pay the indebtedness of MULTI, while at the same time completely disavowing and denying any such obligation. It stressed that should MULTI or Babst be finally adjudged liable under the suretyship agreement, they cannot lawfully recover from ELISCON, but from the DBP which had been substituted as the new debtor.

MULTI filed its Comment,^[29] admitting the correctness of the petition and adopting the Comment of ELISCON insofar as it is not inconsistent with the positions of Babst and MULTI.

At the outset, the preliminary issue of BPIs right of action must first be addressed. ELISCON and MULTI assail BPIs legal capacity to recover their obligation to CBTC. However, there is no question that there was a valid merger between BPI and CBTC. It is settled that in the merger of two existing corporations, one of the corporations survives and continues the business, while the other is dissolved and all its rights, properties and liabilities are acquired by the surviving corporation.^[30] Hence, BPI has a right to institute the case *a quo*.

We now come to the primordial issue in this case whether or not BPI consented to the assumption by DBP of the obligations of ELISCON.

Article 1293 of the Civil Code provides:

Novation which consists in substituting a new debtor in